

**TREASURY MANAGEMENT STRATEGY STATEMENT, TREASURY MANAGEMENT POLICY STATEMENT, MINIMUM REVENUE PROVISION POLICY STATEMENT AND ANNUAL INVESTMENT STATEMENT 2012/13**

**Purpose**

To comply with the requirement of the Council's Treasury Management Policy in reporting to Council the proposed strategy for the forthcoming year and the Local Government Act 2003 with the reporting of the Prudential Indicators.

**Executive Summary**

The Local Government Act 2003 (LGA 2003) requires the Council to produce prudential indicators in line with the Prudential Code.

This report outlines the Council's prudential indicators for 2012/13 – 2014/15 and sets out the expected Treasury operations for this period. This report and associated tables fulfil the statutory requirement of the LGA 2003 by:

- Reporting the prudential indicators as required by the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code for Capital Finance in Local Authorities;
- Setting the Council's Minimum Revenue Provision (MRP) Policy, which defines how the Council will pay for capital assets through revenue contributions each year (as required by Regulation under the Local Government and Public Involvement in Health Act 2007);
- Setting the Treasury Management Strategy in accordance with the CIPFA Code of Practice on Treasury Management;
- Adopts the Council's Treasury Management Policy Statement as recommended within the CIPFA Code of Practice 2011;
- Setting the Investment Strategy (in accordance with the Department for Communities and Local Government (CLG) investment guidance);
- Affirming the effective management and responsibility for the control of risk and clearly identify our appetite for risk. The Authority's risk appetite is low in order to give priority to **Security, Liquidity then Yield** (or return on investments).

The main issues for Members to note are:

1. The CIPFA Code of Practice and associated Guidance Notes adopted by the Council in February 2010 require that:
  - Credit ratings should only be used as a starting point when considering risk. Use should also be made of market data and information, the quality financial press, information on government support for banks and the credit ratings of that government support;
  - There needs to be, at a minimum, a mid year review of Treasury Management Strategy and Performance. The review is intended to highlight any areas of concern that have arisen since the original strategy was approved;
  - Each Council must delegate the role of scrutiny of Treasury Management Strategy and policies to a specific named body – the Audit and Governance Committee has been given this role;
  - Members should be provided with access to relevant training – Members are also personally responsible for ensuring they have the necessary skills and training.

The aim is for all Members to have ownership and understanding when making decisions on Treasury Management matters.

2. With regard to Counterparty selection for investment, rather than adopt a Lowest Common Denominator (LCD) methodology, a broader counterparty evaluation criteria is used by Sector (the Council's Treasury Management consultants). This methodology has been progressively enhanced over the last year and now uses a sophisticated modelling approach with credit ratings from all three rating agencies forming the core element – but in line with best practice/guidance also includes the following as overlays: -
  - credit watches and credit outlooks from credit rating agencies;
  - Credit Default Swap (CDS) spreads to give early warning of likely changes in credit ratings;
  - Sovereign ratings to select counterparties from only the most creditworthy countries.

The adoption of the above approach will help mitigate risks associated with the investment portfolio.

3. As agreed in past Treasury Management Strategies, it is proposed that the Council (following consultation with our advisors) will not use the approach suggested by CIPFA of using the lowest common denominator rating from all three rating agencies to determine creditworthy counterparties (as Moodys are currently very much more aggressive in giving low ratings than the other two agencies). The use of the Lowest Common Denominator rating would give the Authority a very restrictive/unworkable counterparty list which would result in a disproportional (high) level of investment in a few institutions which would as a consequence increase investment risk with the investments being held with a limited number of counterparties which would be counter-productive in not allowing the sharing / spreading of risk over a higher number of counterparties. This would therefore be unworkable and leave the Council with few banks on its approved lending list.

The Sector creditworthiness service does though, use ratings from all three agencies, but by using a scoring system, does not give undue importance to just one agency's ratings.

The approach taken in item 2 and 3 above allows officers charged with the Treasury responsibilities to have the most appropriate/market assessment to aid the investment decision making process and provides a broad methodology for identifying High Credit Quality counterparties.

### **Equalities implications**

There are no equalities implications arising from the report.

### **Legal implications**

Approval of Prudential Indicators and an Annual Investment Strategy is a legal requirement of the Local Government Act 2003. Members are required under the CIPFA Code of Practice to have ownership and understanding when making decisions on Treasury Management matters.

### **Resource and Value for Money implications**

All financial resource implications are detailed in the body of this report which links to the Council's Medium Term Financial Strategy.

### **Risk implications**

Risk is inherent in Treasury Management and as such a risk based approach has been adopted throughout the report with regard to Treasury Management processes.

A Glossary of terms utilised within the report can be found at **ANNEX 8**.

### **Report Author**

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<b>Background Papers:-</b>	<b>Local Government Act 2003</b>
	<b>CIPFA Code of Practice on Treasury Management in Public Services 2011</b>
	<b>CLG Guidance on Local Government Investments March 2010</b>
	<b>Annual Treasury Report 2010/11</b>
	<b>Mid-year Treasury Report 2011/12</b>
	<b>Budget &amp; Medium Term Financial Strategy 2012/13</b>
	<b>CLG Housing Determinations and Local Government Finance Settlement 2011/12 &amp; 2012/13</b>
	<b>Treasury Management Practices 2012/13 (Operational Detail)</b>

## **1. Introduction**

### **1.1 The Treasury Management Policy Statement**

This Council defines its Treasury Management activities as:

- The management of the Council's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.
- This organisation regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its Treasury Management activities will be measured. Accordingly, the analysis and reporting of Treasury Management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.
- This organisation acknowledges that effective Treasury Management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in Treasury Management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.
- The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the Treasury Management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.
- The second main function of the Treasury Management service is the funding of the Council's Capital Programmes. These Capital Programmes provide a guide to the borrowing need of the Council, essentially the longer term cash flow planning to ensure that the Council can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

### **1.2 Reporting requirements**

The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals. These reports are required to be adequately scrutinised by a Committee. This role is undertaken by the Audit and Governance Committee.

**i) Prudential and Treasury Indicators and Treasury Strategy** (this report) - The first, and most important report covers:

- the Capital Programmes (including prudential indicators);
- a Minimum Revenue Provision Policy (how residual capital expenditure is charged to revenue over time);
- the Treasury Management Strategy (how the investments and borrowings are to be organised) including Treasury Indicators; and
- an Investment Strategy (the parameters on how investments are to be managed).

**ii) A Mid Year Treasury Management Report** – This will update Members with the progress of the capital position, amending prudential indicators as necessary, and detail whether Treasury operations comply with the Strategy or whether any policies require revision.

**iii) An Annual Treasury Report** – This provides details of a selection of actual Prudential and Treasury Indicators and actual Treasury Operations compared to the estimates within the Strategy.

### **1.3 Treasury Management Strategy for 2012/13**

The Strategy for 2012/13 covers two main areas:

#### **a) Capital Issues**

- the Capital Programmes and the Prudential Indicators;
- the MRP Strategy.

#### **b) Treasury Management Issues**

- the current treasury position;
- treasury indicators which will limit the treasury risk and activities of the Council;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy; and
- policy on use of external service providers.

These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, the CLG MRP Guidance, the CIPFA Treasury Management Code and the CLG Investment Guidance.

## **2. The Capital Prudential Indicators 2012/13 – 2014/15**

The Council's capital expenditure plans are the key driver of Treasury Management activity. The output of the capital expenditure plans are reflected in prudential indicators, which are designed to assist Members' overview and confirm Capital Expenditure plans.

A key issue facing the Council is the impact of planned HRA Reform. This would essentially end the impact of the Housing Subsidy System and will see the HRA as a stand alone business.

The Council currently pays into the HRA Housing Subsidy System, and in order to stop future payments from 1 April 2012 the Council is required to pay the CLG £44.668m. This payment is effectively HRA debt, and so the prudential indicators have been adjusted to reflect this change. The actual payment will be made on the 28 March 2012 and so the indicators will take immediate effect from the approval of these limits by Council. The change is expected to be beneficial to the Council.

**a) Capital Expenditure.** This prudential Indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle:

<b>Capital Expenditure</b>	<b>2010/11 Actual</b>	<b>2011/12 Probable Outturn</b>	<b>2012/13 Estimate</b>	<b>2013/14 Estimate</b>	<b>2014/15 Estimate</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
<b>Non-HRA</b>	<b>1.273</b>	<b>0.883</b>	<b>3.145*</b>	<b>2.944</b>	<b>0.521</b>
HRA existing	4.352	4.450	7.816	7.550	7.739
HRA settlement	-	44.668	-	-	-
<b>HRA</b>	<b>4.352</b>	<b>49.118</b>	<b>7.816</b>	<b>7.550</b>	<b>7.739</b>
<b>Total</b>	<b>5.625</b>	<b>50.001</b>	<b>10.961</b>	<b>10.494</b>	<b>8.260</b>

\* includes projected slippage from 2011/12

- Other long term liabilities. The above financing need, excludes other long term liabilities, such as Private Finance Initiatives (PFI) and leasing arrangements which already include borrowing instruments.

The table below summarises the above capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding need (borrowing).

<b>Capital Expenditure</b>	<b>2010/11 Actual</b>	<b>2011/12 Probable Outturn</b>	<b>2012/13 Estimate</b>	<b>2013/14 Estimate</b>	<b>2014/15 Estimate</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
Non-HRA	1.273	0.883	3.145	2.944	0.521
HRA	4.352	4.450	7.816	7.550	7.739
HRA settlement	-	44.668	-	-	-
<b>Total</b>	<b>5.625</b>	<b>50.001</b>	<b>10.961</b>	<b>10.494</b>	<b>8.260</b>
<b>Financed by:</b>					
Capital receipts	0.877	0.462	1.029	0.213	0.176
Capital grants	0.559	0.421	1.324	2.422	0.295
Capital reserves	0.908	1.617	1.098	0.300	0.050
Revenue	2.801	2.833	7.510	7.559	7.739
<b>Total</b>	<b>5.145</b>	<b>5.333</b>	<b>10.961</b>	<b>10.494</b>	<b>8.260</b>
<b>Net financing need for the year</b>	<b>0.480</b>	<b>44.668</b>	<b>-</b>	<b>-</b>	<b>-</b>

## **b) The Council's Borrowing Need (the Capital Financing Requirement)**

The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need. Any capital expenditure above, which has not immediately been paid for, will increase the CFR.

The Council is asked to approve the CFR projections below:

<b>CFR Projections</b>	<b>2010/11 Actual £m</b>	<b>2011/12 Estimate £m</b>	<b>2012/13 Estimate £m</b>	<b>2013/14 Estimate £m</b>	<b>2014/15 Estimate £m</b>
<b>Capital Financing Requirement</b>					
CFR – Non-HRA	3.833	0.429*	0.412	0.396	0.380
CFR - HRA	23.395	23.395	68.063	68.063	68.063
HRA Settlement	-	44.668	-	-	-
<b>Total CFR</b>	<b>27.228</b>	<b>68.492</b>	<b>68.475</b>	<b>68.459</b>	<b>68.443</b>
<b>Movement in CFR (increase / (decrease))</b>	<b>0.286</b>	<b>41.264</b>	<b>(0.017)</b>	<b>(0.016)</b>	<b>(0.016)</b>

<b>Movement in CFR represented by</b>					
Net financing need for the year (above)	0.480	-	-	-	-
HRA Settlement	-	44.668	-	-	-
Less MRP/VRP and other financing movements	(0.194)	(3.404)*	(0.017)	(0.016)	(0.016)
<b>Movement in CFR (increase / (decrease))</b>	<b>0.286</b>	<b>41.264</b>	<b>(0.017)</b>	<b>(0.016)</b>	<b>(0.016)</b>

\* Assumes reversal of estimated Capitalisation Directive of £3.386m re anticipated Icelandic Banking receipt – actual figure subject to finalisation as part of Annual Accounts production

### c) MRP Policy Statement

The Council is required to pay off an element of the accumulated General Fund capital spend each year (the CFR) through a revenue charge (the Minimum Revenue Provision - MRP), although it is also allowed to undertake additional voluntary payments if required (Voluntary Revenue Provision - VRP).

CLG Regulations have been issued which require the full Council to approve **an MRP Statement** in advance of each year. A variety of options are provided to councils, so long as there is a prudent provision. The Council is recommended to approve the following MRP Statement:

For capital expenditure incurred before 1 April 2008 or which in the future will be Supported Capital Expenditure, the MRP policy will be:

- **Existing practice** - MRP will follow the existing practice outlined in former CLG regulations (option 1);

These options provide for an approximate 4% reduction in the borrowing need (CFR) each year.

From 1 April 2008 for all unsupported borrowing (including PFI and finance leases) the MRP policy will be:

- **Asset Life Method** – MRP will be based on the estimated life of the assets, in accordance with the proposed regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction) (option 3);

These options provide for a reduction in the borrowing need over approximately the asset's life.

No revenue charge is currently required for the HRA. However under HRA reform the HRA will be required to charge depreciation on its assets, which will have a revenue effect. In order to address any possible adverse impact, regulations will allow the Major Repairs Allowance to be used as a proxy for depreciation for the first five years.

#### d) The Use of the Council's Resources and the Investment Position

The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.). Detailed below are estimates of the year end balances for each resource and anticipated day to day cash flow balances.

Year End Resources	2010/11 Actual £m	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
Fund balances	9.598	8.920	7.029	5.555	3.969
Capital receipts	1.907	1.445	0.416	0.202	0.026
Earmarked Reserves	7.237	5.279	4.179	3.895	3.845
Other	0.048	-	-	-	-
<b>Total Core Funds</b>	<b>18.790</b>	<b>15.644</b>	<b>11.624</b>	<b>9.652</b>	<b>7.840</b>
Working capital*	1.039	0.720	3.403	4.344	5.087
(Under)/over borrowing	(6.836)	(3.432)	(3.415)	(3.399)	(3.383)
<b>Expected Investments</b>	<b>12.993</b>	<b>12.932</b>	<b>11.612</b>	<b>10.597</b>	<b>9.544</b>

\*Working capital balances shown are estimated year end; these may be higher mid year

#### e) Affordability Prudential Indicators

The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances. The Council is asked to approve the following indicators:

**f) Actual and estimates of the ratio of financing costs to net revenue stream.** This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

Fund	2010/11 Actual %	2011/12 Revised Estimate %	2012/13 Estimate %	2013/14 Estimate %	2014/15 Estimate %
Non-HRA	3.70	37.18*	(2.15)	(3.12)	(3.60)
HRA (inclusive of settlement)	(6.91)	(5.41)	15.88	14.27	13.83

\* Assumes one off reversal of estimated Capitalisation Directive of £3.386m re anticipated Icelandic Banking receipt – actual figure subject to finalisation as part of Annual Accounts production

\*\* Shown as (negative) as income exceeds costs

The estimates of financing costs include current commitments and the proposals in this budget report.

#### g) Estimates of the incremental impact of capital investment decisions on council tax.

This indicator identifies the revenue costs associated with proposed changes to the three year capital programme recommended in this budget report compared to the Council's existing approved commitments and current plans. The assumptions are based on the budget, but will invariably include some estimates, such as the level of Government support, which is not published over a three year period.



## Incremental impact of capital investment decisions on the Band D Council Tax

Council tax impact	2010/11 Actual £	2011/12 Estimate £	2012/13 Estimate £	2013/14 Estimate £	2014/15 Estimate £
Council Tax - band D	3.52	1.04	0.28	0.52	0.26

**h) Estimates of the incremental impact of capital investment decisions on housing rent levels.** Similar to the council tax calculation, this indicator identifies the trend in the cost of proposed changes in the housing capital programme recommended in this budget report compared to the Council's existing commitments and current plans, expressed as a discrete impact on weekly rent levels.

## Incremental impact of capital investment decisions on housing rent levels

Housing Rent impact	2010/11 Actual £	2011/12 Estimate £	2012/13 Estimate £	2013/14 Estimate £	2014/15 Estimate £
Weekly housing rent levels	0.05	0.07	0.08	0.13	0.12

This indicator shows the revenue impact on any newly proposed changes, although any discrete impact will be constrained by rent controls.

## 3 . Treasury Management Strategy

The capital expenditure plans set out in Section 2 provide details of the service activity of the Council. The Treasury Management function ensures that the Council's cash is organised in accordance with the the relevant professional codes, so that sufficient cash is available to meet this service activity. This will involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. The strategy covers the relevant treasury / prudential indicators, the current and projected debt positions and the annual investment strategy.

### 3.1 Current Portfolio Position

The Council's Treasury Portfolio position at 31 March 2011, with forward projections are summarised below. The table shows the actual external debt (the Treasury Management Operations), against the underlying capital borrowing need (the Capital Financing Requirement - CFR), highlighting any over or under borrowing.

Current Portfolio	2010/11 Actual £m	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
<b>External Debt</b>					
Debt at 1 April	22.392	20.392	65.060	65.060	65.060
Expected change in Debt	(2.000)	-	-	-	-
HRA settlement	-	44.668	-	-	-
<b>Actual debt at 31 March (A)</b>	<b>20.392</b>	<b>65.060</b>	<b>65.060</b>	<b>65.060</b>	<b>65.060</b>
<b>The Capital Financing Requirement</b>	<b>27.228</b>	<b>68.492</b>	<b>68.475</b>	<b>68.459</b>	<b>68.443</b>
<b>Under / (over) borrowing</b>	<b>6.836</b>	<b>3.432</b>	<b>3.415</b>	<b>3.399</b>	<b>3.383</b>

Current Portfolio	2010/11 Actual £m	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
<b>Total Investments at 31 March</b>					
Investments (B)	12.993*	12.932	11.612	10.597	9.544
Investment change	(0.779)	(0.061)	(1.320)	(1.015)	(1.053)
<b>Net Debt (A-B)</b>	<b>7.399</b>	<b>52.128</b>	<b>53.448</b>	<b>54.463</b>	<b>55.516</b>

*\*Excludes investments 'at risk' with Icelandic Banks*

Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well defined limits. One of these is that the Council needs to ensure that its total borrowing, net of any investments, does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2012/13 and the following two financial years (shown as net borrowing above). This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

The Corporate Director Resources reports that the Council complied with this prudential indicator in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

### 3.2. Treasury Indicators: Limits to Borrowing Activity

**The Operational Boundary** - This is the limit beyond which external borrowing is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, but may be lower or higher depending on the levels of actual borrowing.

Operational boundary	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
Borrowing	27.600	72.268	72.268	72.268
Add HRA settlement	44.668	-	-	-
Other long term liabilities	-	-	-	-
Total	72.268	72.268	72.268	72.268

**The Authorised Limit for external borrowing** - A further key prudential indicator represents a control on the maximum level of borrowing. This represents a limit beyond which external borrowing is prohibited, and this limit needs to be set or revised by the full Council. It reflects the level of external borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term.

1. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.
2. The Council is asked to approve the following Authorised Limit:

Authorised limit	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
Borrowing	33.100	89.112	89.112	89.112
Add HRA settlement	56.012	-	-	-
Other long term liabilities	3.000	3.000	3.000	3.000
Total	92.112*	92.112	92.112	92.112

*\* Includes £79.407m HRA Self Financing Cap – Including Headroom of £11.344m.*

Separately, the Council is also limited to a maximum HRA CFR through the HRA self-financing regime. This limit is currently:

HRA Debt Limit	2011/12 Estimate £m	2012/13 Estimate £m	2013/14 Estimate £m	2014/15 Estimate £m
Total	79.407	79.407	79.407	79.407

### 3.3. Prospects for Interest Rates

The Council has appointed Sector as its treasury advisor and part of their service is to assist the Council to formulate a view on interest rates. **ANNEX 1** draws together a number of current City forecasts for short term (Bank Rate) and longer fixed interest rates. The following table gives the Sector central view.

Annual Average	Bank Rate %	Money Rates		PWL B Borrowing Rates		
		3 month %	1 year %	5 year %	25 year %	50 year %
March 2012	0.50	0.70	1.50	2.30	4.20	4.30
June 2012	0.50	0.70	1.50	2.30	4.20	4.30
Sept 2012	0.50	0.70	1.50	2.30	4.30	4.40
Dec 2012	0.50	0.70	1.60	2.40	4.30	4.40
March 2013	0.50	0.75	1.70	2.50	4.40	4.50
June 2013	0.50	0.80	1.80	2.60	4.50	4.60
Sept 2013	0.75	0.90	1.90	2.70	4.60	4.70
Dec 2013	1.00	1.20	2.20	2.80	4.70	4.80
March 2014	1.25	1.40	2.40	2.90	4.80	4.90
June 2014	1.50	1.60	2.60	3.10	4.90	5.00

Growth in the UK economy is expected to be weak in the next two years and there is a risk of a technical recession (i.e. two quarters of negative growth). Bank Rate, currently 0.5%, underpins investment returns and is not expected to start increasing until Quarter 3 of 2013 despite inflation currently being well above the Monetary Policy Committee inflation target. Hopes for an export led recovery appear likely to be disappointed due to the Eurozone sovereign debt crisis depressing growth in the UK's biggest export market. The Comprehensive Spending Review, which seeks to reduce the UK's annual fiscal deficit, will also depress growth during the next few years.

Fixed interest borrowing rates are based on UK gilt yields. The outlook for borrowing rates is currently much more difficult to predict. The UK total national debt is forecast to continue rising until 2015/16; the consequent increase in gilt issuance is therefore expected to be reflected in an increase in gilt yields over this period. However, gilt yields are currently at historically low levels due to investor concerns over Eurozone sovereign debt and have been subject to exceptionally high levels of volatility as events in the Eurozone debt crisis have evolved.

This challenging and uncertain economic outlook has several key treasury management implications:

- The Eurozone sovereign debt difficulties, most evident in Greece, provide a clear indication of much higher counterparty risk. This continues to suggest the use of higher quality counterparties for shorter time periods;
- Investment returns are likely to remain relatively low during 2012/13;
- Borrowing interest rates are currently attractive, but may remain low for some time. The timing of any borrowing will need to be monitored carefully;
- There will remain a cost of capital – any borrowing undertaken that results in an increase in investments will incur a revenue loss between borrowing costs and investment returns.

### 3.4 Borrowing Strategy

The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is high and will be maintained for the borrowing excluding the HRA reform settlement.

Against this background and the risks within the economic forecast, caution will be adopted with the 2012/13 treasury operations. The Corporate Director Resources will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- *if it was felt that there was a significant risk of a sharp FALL in long and short term rates, e.g. due to a marked increase of risks around relapse into recession or of risks of deflation, then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.*
- *if it was felt that there was a significant risk of a much sharper RISE in long and short term rates than that currently forecast, perhaps arising from a greater than expected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates were still relatively cheap.*

The requirement for the HRA reform settlement to be made to the CLG on 28 March 2012 will require a separate consideration of a borrowing strategy. The Council will need to have the cash settlement amount of £44.668m available by the 28<sup>th</sup> March 2012, so separate borrowing solely for this purpose is anticipated. The PWLB are providing loans at interest rates 0.85% lower than the usual PWLB interest rates solely for the settlement requirements. This provides a compelling reason to utilise this borrowing availability. The exact structure of debt to be drawn is currently being considered by officers to ensure it meets the requirements of the HRA business plan and the overall requirements of the Council. Whilst the debt can be drawn earlier than needed, this may incur a revenue cost, and will be considered when a review of the structure of actual prevailing borrowing and investment interest rates is undertaken nearer to the time.

Any decisions will be reported to the appropriate decision making body at the next available opportunity.

Following detailed review of the business plan and after consultation with our Treasury consultants (Sector) the Treasury management team are proposing to fund the settlement payment by taking loans from the Public Works Loans Board (PWLB). Up to ten individual loans with a long term maturity pattern of 40 to 50 years will be taken and debt for the HRA will be held separately from General Fund under a two pool option. It is also proposed to continue with the use of internal resources to fund the difference between the new Capital Financing Requirement and the new levels of borrowing resulting from the reform. This will benefit both the HRA and General Fund as the special rate would not be available for this debt and it would also reduce the overall level of exposure for Council investments.

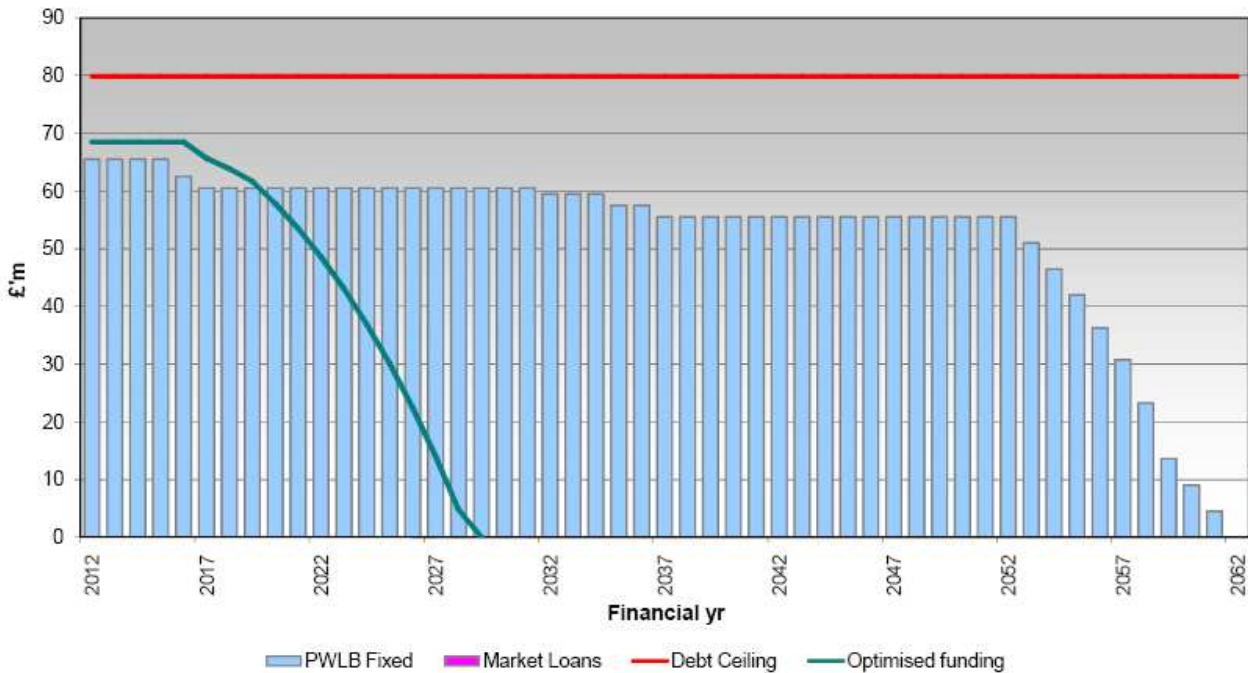
This approach has been adopted based on the following factors;

- By taking advantage of the PWLB special terms mentioned above, the Authority will obtain a lower rate and at a lower cost than currently available from other sources.
- By breaking down the sum required into smaller individual loans, this will make the debt more manageable and flexible should circumstances/priorities change.
- By taking long term loans, the HRA will have certainty over its borrowing costs throughout and past the business plan period.

The graph below shows a comparison of the debt ceiling, outstanding loans within the housing pool (as per the two pool option) and optimised funding levels. All existing debt would become Housing debt. The vertical bars show the outstanding loans in the housing pool for each year and the red line at the top shows the debt ceiling or cap for the Authority as determined by the CLG. The green line shows the optimised funding level from the PwC LA model, or in other words, the loans outstanding after taking account of surpluses in the business plan to repay loans.

As you can see, beyond 2020, the Authority has outstanding loans above the funding requirement identified from the business plan. This allows the Authority to have some flexibility within its housing capital expenditure plans (for redevelopment etc.) in the future.

**Housing Loans Outstanding compared to Optimised Funding Levels**



### Treasury Management Limits on Activity

There are three debt related treasury activity limits. The purpose of these are to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates. However, if these are set to be too restrictive they will impair the opportunities to reduce costs / improve performance. The indicators are:

- Upper limits on variable interest rate exposure. This identifies a maximum limit for variable interest rates based upon the debt position net of investments;
- Upper limits on fixed interest rate exposure. This is similar to the previous indicator and covers a maximum limit on fixed interest rates;
- Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing, and are required for upper and lower limits.

The Council is asked to approve the following treasury indicators and limits:

<b>Year:</b>	<b>2012/13 £m</b>	<b>2013/14 £m</b>	<b>2014/15 £m</b>
<b>Interest rate Exposures</b>			
	<b>Upper</b>	<b>Upper</b>	<b>Upper</b>
<b>Limits on fixed interest rates based on net debt</b>	58	58	58
<b>Limits on variable interest rates based on net debt</b>	7	7	7
<b>Maturity Structure of fixed interest rate borrowing 2012/13</b>			
	<b>Lower</b>	<b>Upper</b>	
Under 12 months	0%	20%	
12 months to 2 years	0%	20%	
2 years to 5 years	0%	25%	
5 years to 10 years	0%	75%	
10 years and above	0%	100%	

### **3.5 Policy on Borrowing in Advance of Need**

The Council will not borrow more than, or in advance of, its needs, purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates, and will be considered carefully to ensure that value for money can be demonstrated and that the Council can ensure the security of such funds.

Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

### **3.6. Debt Rescheduling**

As short term borrowing rates will be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

The reasons for any rescheduling to take place will include:

- the generation of cash savings and / or discounted cash flow savings;
- helping to fulfil the treasury strategy;
- enhancing the balance of the portfolio (amend the maturity profile and/or the balance of volatility).

Consideration will also be given to identify if there is any residual potential for making savings by running down investment balances to repay debt prematurely as short term rates on investments are likely to be lower than rates paid on current debt.

All rescheduling will be reported to Council, at the earliest meeting following its action.

## 3.7. Annual Investment Strategy

### 3.7.1 Investment Policy

The Council's investment policy has regard to the CLG's Guidance on Local Government Investments ("the Guidance") and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The Council's investment priorities will be security first, liquidity second, then return.

In accordance with guidance from the CLG and CIPFA, and in order to minimise the risk to investments, the Council has below clearly stipulated the minimum acceptable credit quality of counterparties for inclusion on the lending list. The creditworthiness methodology used to create the counterparty list fully accounts for the ratings, watches and outlooks published by all three ratings agencies with a full understanding of what these reflect in the eyes of each agency. Using the Sector ratings, service banks' ratings are monitored on a real time basis with knowledge of any changes notified electronically as the agencies notify modifications.

Further, the Council's officers recognise that ratings should not be the sole determinant of the quality of an institution and that it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To this end the Council will engage with its advisors to maintain a monitor on market pricing such as "Credit Default Swaps" and overlay that information on top of the credit ratings. This is fully integrated into the credit methodology provided by the advisors, Sector, in producing its colour codings which show the varying degrees of creditworthiness.

Other information sources used will include the financial press, share price and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

The aim of the strategy is to generate a list of highly creditworthy counterparties which will also enable diversification and thus avoidance of concentration risk.

The intention of the strategy is to provide security of investment and minimisation of risk.

Investment instruments identified for use in the financial year are listed in **ANNEX 3** under the 'Specified' and 'Non-Specified' Investments categories. Counterparty limits will be as set through the Council's Treasury Management Practices – Schedules.

Investment instruments identified for use in the financial year are listed in **ANNEX 3** under the 'Specified' and 'Non-Specified' Investments categories. Counterparty limits will be as set through the Council's Treasury Management Practices – Schedules.

### 3.7.2 Creditworthiness policy

This Council applies the creditworthiness service provided by Sector. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moodys and Standard and Poors. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- CDS spreads to give early warning of likely changes in credit ratings;
- sovereign ratings to select counterparties from only the most creditworthy countries.

This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties.

These colour codes are used by the Council to determine the duration for investments. The Council will therefore use counterparties within the following durational bands:

- Yellow 5 years \*
- Purple 2 years
- Blue 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange 1 year
- Red 6 months
- Green 3 months
- No Colour not to be used

*\* this category is for AAA rated Government debt or its equivalent; please also see collateralised deposits added into ANNEX 3 as an investment instrument.*

The Sector creditworthiness service uses a wider array of information than just primary ratings and by using a risk weighted scoring system, does not give undue preponderance to just one agency's ratings.

Typically the minimum credit ratings criteria the Council use will be a short term rating (Fitch or equivalents) of Short Term rating F1, Long Term rating A-, Viability ratings of BB+, and a Support rating of 3. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

All credit ratings will be monitored on a daily basis/as and when notified. The Council is alerted to changes to ratings of all three agencies through its use of the Sector creditworthiness service.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Council will be advised of information in movements in Credit Default Swap against the iTraxx benchmark and other market data on a weekly basis. Extreme market movements may result in downgrade of an institution or removal from the Council's lending list.

Sole reliance will not be placed on the use of this external service. In addition this Council will also use market data and market information, information on government support for banks and the credit ratings of that government support.

### **3.7.3 Country limits**

The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AAA from Fitch (or equivalent). The list of countries that qualify using this credit criteria as at the date of this report are shown in **ANNEX 4**. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

Sector also recommends that no more than 20% of the Council's investment portfolio should be placed with an individual counterparty, in order to spread risk. The approach at the Council is to set monetary limits of up to £4m with individual institutions, which equates approximately to Sector's recommendation (based on current average investment levels).



### 3.7.4 Investment Strategy

**a) In-house funds.** Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

**b) Investment returns expectations.** Bank Rate is forecast to remain unchanged at 0.5% before starting to rise from quarter 3 of 2013. Bank Rate forecasts for financial year ends (March) are:

- 2011/ 2012 0.50%
- 2012/ 2013 0.50%
- 2013/ 2014 1.25%
- 2014/ 2015 2.50%

There are downside risks to these forecasts (i.e. start of increases in Bank Rate is delayed even further) if economic growth remains weaker for longer than expected. However, should the pace of growth pick up more sharply than expected there could be upside risk, particularly if Bank of England inflation forecasts for two years ahead exceed the Bank of England's 2% target rate.

Sector's suggested budgeted investment earnings rates for returns on investments placed for periods up to three months during each financial year for the next five years are as follows:

- 2012/2013 0.70%
- 2013/2014 1.00%
- 2014/2015 1.60%
- 2015/2016 3.30%
- 2016/2017 4.10%

**c) Investment treasury indicator and limit** - total principal funds invested for greater than 364 days. These limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment, and are based on the availability of funds after each year-end.

The Council is asked to approve the treasury indicator and limit: -

<b>Maximum principal sums invested &gt; 364 days</b>			
<b>Year:</b>	<b>2012/13</b>	<b>2013/14</b>	<b>2014/15</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>
Principal sums invested > 364 days	3.0	2.5	2.0

For its cash flow generated balances, the Council will seek to utilise its business reserve accounts, Call accounts and 15 and 30 day notice accounts, money market funds and short-dated deposits (overnight to three months) in order to benefit from the compounding of interest.

### 3.7.5 Icelandic Bank Investments

The Icelandic courts have supported the view that the Councils' investments in Glitnir will be treated as a preferred creditor, thereby seeing a high proportion of the investment being returned. The actual repayment is currently expected to be partially in foreign currency assets. It is currently too early to provide a definitive policy on how this exchange rate risk will be managed, but the expectation will be that the risk will be managed proactively and assets converted to sterling at the earliest opportunity. We are currently still receiving dividend distributions from the administrators of Heritable and Kaupthing Singer & Friedlander with anticipated total recoveries of 85% and 82% respectively.

### **3.8 End of year investment report**

At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

### **3.9 Policy on the use of external service providers**

The Council uses Sector as its external Treasury Management advisors.

The Council recognises that responsibility for Treasury Management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

It also recognises that there is value in employing external providers of Treasury Management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

### **3.10 Scheme of delegation**

Please see **ANNEX 5**.

### **3.11 Role of the Section 151 Officer**

Please see **ANNEX 6**.

## Annexes

Annex
1. Interest Rate Forecasts
2. Economic Background
3. Specified and Non-Specified Investments
4. Approved Countries for investments
5. Treasury Management Scheme of Delegation
6. The Treasury Management Role of the Section 151 Officer
7. Treasury Management Practices
8. Treasury Management Glossary of Terms

## Interest Rate Forecasts 2011 - 2015

Sector's Interest Rate View															
	Now	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Sep-14	Dec-14	Mar-15
<b>Sector's Bank Rate View</b>	<b>0.50%</b>	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	2.00%	2.25%	2.50%
<b>3 Month LIBID</b>	<b>0.87%</b>	0.70%	0.70%	0.70%	0.70%	0.70%	0.75%	0.80%	0.90%	1.20%	1.40%	1.60%	2.10%	2.40%	2.60%
<b>6 Month LIBID</b>	<b>1.16%</b>	1.00%	1.00%	1.00%	1.00%	1.00%	1.10%	1.20%	1.40%	1.60%	1.80%	2.00%	2.50%	2.70%	2.90%
<b>12 Month LIBID</b>	<b>1.65%</b>	1.50%	1.50%	1.50%	1.50%	1.60%	1.70%	1.80%	1.90%	2.20%	2.40%	2.60%	3.10%	3.20%	3.30%
<b>5yr PWLB Rate</b>	<b>2.25%</b>	2.30%	2.30%	2.30%	2.30%	2.40%	2.50%	2.60%	2.70%	2.80%	2.90%	3.10%	3.30%	3.50%	3.70%
<b>10yr PWLB Rate</b>	<b>3.33%</b>	3.30%	3.30%	3.30%	3.40%	3.40%	3.50%	3.60%	3.70%	3.80%	4.00%	4.20%	4.40%	4.60%	4.80%
<b>25yr PWLB Rate</b>	<b>4.24%</b>	4.20%	4.20%	4.20%	4.30%	4.30%	4.40%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.20%
<b>50yr PWLB Rate</b>	<b>4.26%</b>	4.30%	4.30%	4.30%	4.40%	4.40%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.20%	5.30%
<b>Bank Rate</b>															
<b>Sector's View</b>	<b>0.50%</b>	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	2.00%	2.25%	2.50%
<b>UBS</b>	<b>0.50%</b>	0.50%	0.50%	0.50%	0.50%	0.50%	-	-	-	-	-	-	-	-	-
<b>Capital Economics</b>	<b>0.50%</b>	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	-	-	-	-	-
<b>5yr PWLB Rate</b>															
<b>Sector's View</b>	<b>2.25%</b>	2.30%	2.30%	2.30%	2.30%	2.40%	2.50%	2.60%	2.70%	2.80%	2.90%	3.10%	3.30%	3.50%	3.70%
<b>UBS</b>	<b>2.25%</b>	-	-	-	-	-	-	-	-	-	-	-	-	-	-
<b>Capital Economics</b>	<b>2.25%</b>	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%	-	-	-	-	-
<b>10yr PWLB Rate</b>															
<b>Sector's View</b>	<b>3.33%</b>	3.30%	3.30%	3.30%	3.40%	3.40%	3.50%	3.60%	3.70%	3.80%	4.00%	4.20%	4.40%	4.60%	4.80%
<b>UBS</b>	<b>3.33%</b>	3.45%	3.45%	3.50%	3.60%	3.65%	-	-	-	-	-	-	-	-	-
<b>Capital Economics</b>	<b>3.33%</b>	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	-	-	-	-	-
<b>25yr PWLB Rate</b>															
<b>Sector's View</b>	<b>4.24%</b>	4.20%	4.20%	4.20%	4.30%	4.30%	4.40%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.20%
<b>UBS</b>	<b>4.24%</b>	4.80%	4.90%	4.90%	4.90%	4.90%	-	-	-	-	-	-	-	-	-
<b>Capital Economics</b>	<b>4.24%</b>	4.30%	4.30%	4.30%	4.30%	4.30%	4.30%	4.30%	4.30%	4.30%	-	-	-	-	-
<b>50yr PWLB Rate</b>															
<b>Sector's View</b>	<b>4.26%</b>	4.30%	4.30%	4.30%	4.40%	4.40%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%	5.10%	5.20%	5.30%
<b>UBS</b>	<b>4.26%</b>	4.80%	4.95%	4.95%	5.00%	5.00%	-	-	-	-	-	-	-	-	-
<b>Capital Economics</b>	<b>4.26%</b>	4.40%	4.40%	4.40%	4.40%	4.40%	4.40%	4.40%	4.40%	4.40%	-	-	-	-	-

## Economic Background

### 4.1. Global Economy

The outlook for the global economy remains clouded with uncertainty with the UK economy struggling to generate sustained recovery that offers solid optimism for the outlook for 2012, or possibly even into 2013. Consumer and business confidence levels are low and with little to boost sentiment, it is not easy to see potential for a significant increase in the growth rate in the short term.

At the centre of much of the uncertainty is the ongoing **Eurozone sovereign debt crisis** which has intensified, rather than dissipated throughout 2011. The main problem has been **Greece**, where, even with an Eurozone/IMF/ECB bailout package and the imposition of austerity measures aimed at deficit reduction, the lack of progress and the ongoing deficiency in addressing the underlying lack of competitiveness of the Greek economy, has seen an escalation of their problems. These look certain to result in a default of some kind but it currently remains unresolved if this will be either “orderly” or “disorderly”. Most commentators currently view that it is now inevitable that Greece will have to exit the Eurozone in 2012.

There is also growing concern about the situation in **Italy** and the risk that contagion has not been contained. Italy is the third biggest debtor country in the world but its prospects are limited given the poor rate of economic growth over the last decade and likely difficulties in implementing the required level of fundamental reforms in the economy. The Eurozone now has a well established track record of always doing too little too late to deal with this crisis; this augurs poorly for future prospects, especially given the rising level of electoral opposition in northern EU countries to bailing out profligate southern countries.

The US economy has encouraged with some positive news around the start of 2012 but any improvement in the weak rate of growth is likely to only generate slow progress in reducing the high level of unemployment which is acting as such a dampener on the economy. With Presidential elections due in November 2012, the current administration has been hamstrung by political gridlock with the two houses split between the main parties. In quarter 3 the Federal Reserve started “Operation Twist” in an effort to re-ignite the rate of growth in the economy. However, high levels of consumer indebtedness, a moribund housing market together with stubbornly high unemployment, will continue to weigh heavily on consumer confidence and so on the ability to generate a healthy and consistent rate of economic growth.

Hopes for broad based recovery have, therefore, focussed on the **emerging markets** but these areas have been struggling with inflationary pressures in their previously fast growth economies. China, though, has maintained its growth pattern, despite a major thrust to tighten monetary policy during 2011 to cool inflationary pressures which are now subsiding. However, some forward looking indicators are causing concern that there may not be a soft landing ahead, which would then be a further dampener on world economic growth.

### 4.2 UK economy

The Government’s austerity measures, aimed at getting the public sector deficit into order over the next four years, have yet to fully impact on the economy. However, coming at a time when economic growth has been weak and concerns at the risk of a technical recession (two quarters of negative growth) in 2012, it looks likely that the private sector will not make up for the negative impact of these austerity measures given the lack of an export led recovery due to the downturn in our major trading partner – the EU. The housing market, a gauge of consumer confidence, remains weak and the outlook is for house prices to be little changed for a prolonged period.

**a) Economic Growth.** GDP growth has, basically, flatlined since the election of 2010 and, worryingly, the economic forecasts for 2012 and beyond have been revised lower on a near

quarterly basis. With concerns of a potential return to recession, the Bank of England embarked on a second round of Quantitative Easing to stimulate economic activity. It appears very likely that there will be another expansion of quantitative easing in quarter 1 2012 in order to stimulate economic growth.

**b) Unemployment.** With the impact of the Government's austerity strategy resulting in steadily increasing unemployment during 2011, there are limited prospects for any improvement in 2012 given the prospects for weak growth.

**c) Inflation and Bank Rate.** For the last two years, the MPC's contention has been that high inflation was the outcome of temporary external factors and other one offs (e.g. changes in VAT); that view remains in place with CPI inflation starting quarter 1 of 2012 at 4.8%, having peaked at 5.2% in September 2011. They remain of the view that the rate will fall back to, or below, the 2% target level within the two year horizon.

**d) AAA rating.** The ratings agencies have recently reaffirmed the UK's AAA sovereign rating and have expressed satisfaction with Government policy for deficit reduction. They have, though, warned that this could be reviewed if the policy were to change, or was seen to be failing to achieve its desired outcome. This credit position has ensured that the UK government is able to fund itself at historically low levels and, with the safe haven status from Eurozone debt also drawing in external investment, the pressure on rates has been down, and looks set to remain so for some time.

### **4.3 Sector's forward view**

Economic forecasting remains troublesome with so many external influences weighing on the UK. There does, however, appear to be consensus among analysts that the economy remains weak and whilst there is still a broad range of views as to potential performance, they have all been downgraded throughout 2011. Key areas of uncertainty include:

- a worsening of the Eurozone debt crisis and heightened risk of the breakdown of the bloc or even of the currency itself;
- the impact of the Eurozone crisis on financial markets and the banking sector;
- the impact of the Government's austerity plan on confidence and growth and the need to rebalance the economy from services to exporting manufactured goods;
- the under-performance of the UK economy which could undermine the Government's policies that have been based upon levels of growth that increasingly seem likely to be undershot;
- a continuation of high levels of inflation ;
- the economic performance of the UK's trading partners, in particular the EU and US, with some analysts suggesting that recession could return to both;
- stimulus packages failing to stimulate growth;
- elections due in the US, Germany and France in 2012 or 2013;
- potential for protectionism i.e. an escalation of the currency war / trade dispute between the US and China.

The overall balance of risks remains weighted to the downside. Lack of economic growth, both domestically and overseas, will impact on confidence putting upward pressure on unemployment. It will also further knock levels of demand which will bring the threat of recession back into focus.

Sector believes that the longer run trend is for gilt yields and PWLB rates to rise due to the high volume of gilt issuance in the UK, and the high volume of debt issuance in other major western countries.

Given the weak outlook for economic growth, Sector sees the prospects for any interest rate changes before mid-2013 as very limited. There is potential for the start of Bank Rate increases to be even further delayed if growth disappoints.

## Specified and Non-Specified Investments:

### 1. Specified Investments:

These investments are **sterling** denominated investments of **not more than one-year maturity**, meeting the minimum 'high' quality criteria where applicable. They are of relatively high security, high liquidity and are low risk assets where the possibility of loss of principal or investment income is small, they could be for a longer period but where the Council has the right to be repaid within 12 months if it wishes. The investments could be managed In-House or by Fund Managers.

These would include investments with:

- The UK Government (such as the Debt Management Office, UK Treasury Bills or Gilts with less than one year to maturity).
- A Local Authority, Parish Council or Community Council.
- Pooled investment vehicles or Collective Investment Schemes structured as Open Ended Investment Companies (OEIC's) such as Money Market Funds (MMF's) Government Liquidity Funds, Enhanced Cash Funds, Bond Funds (but not Corporate Bonds) and Gilt Funds, that have a high credit quality and been awarded a high credit rating of AAA by Standard and Poor's, Moody's or Fitch rating agencies and a Low Long Term Volatility rating.
- A body that has a high credit quality and been awarded a high credit rating by a credit rating agency (such as a bank or building society) and complies with the Sector Credit Worthiness service.
- A body which has been provided with a government issued guarantee for wholesale deposits within specific timeframes and/or is part or wholly nationalised by that Government. Where these guarantees are in place and the government has an AAA sovereign long term rating these institutions will be included within the Council's criteria temporarily until such time as the ratings improve or the guarantees are withdrawn. Monies will only be deposited within the timeframe of the guarantee.

SPECIFIED INVESTMENTS	Minimum 'High' Credit Criteria	Limits
UK Government/ Debt Management Agency Deposit Facility	Defined by Regulation UK Treasury (AAA)	£4m
Term deposits – Local Authorities	Defined by Regulation (Sec 23 of the 2003 act)	£4m
Treasury Bills	Defined by Regulation UK Treasury (AAA)	£4m
Term deposits and Callable deposits – Banks and Building Societies	In accordance with Sector's Creditworthiness Service up to 'Orange' or 'Blue'	£4m individual institutions £6m Group limit
Pooled investment vehicles *(OEIC's, MMF's etc)	AAA (Moody's MR1+, Fitch MMF and S&P M).	£4m
Banks and Building Societies – Forward deals up to 1 year from arrangement to maturity	In accordance with Sector's Creditworthiness Service up to 'Orange' or 'Blue'	£4m

\*For pooled investment vehicles or Collective Investment Schemes (such as MMF's) that have a high credit quality and have been rated AAA by Standard and Poor's, Moody's or Fitch rating agencies and have a Constant Net Asset Value (CNAV).



## 2. Non-Specified Investments:

Non-specified investments are any other type of investment (i.e. not defined as Specified above) and could be managed In-House or by Fund Managers. The identification and rationale supporting the selection of these other investments and the maximum limits to be applied are set out below. Non specified investments would include any sterling investments with:

	<b>Non Specified Investment Categories</b>	<b>Credit Rating</b>	<b>Comment</b>
1	<p><b>Supranational Bonds greater than 1 year to maturity</b></p> <ul style="list-style-type: none"> <li>• <b>Multilateral development bank bonds</b> – These are bonds defined as an international financial institution having as one of its objects economic development, either generally or in any region of the world (e.g. European Investment Bank etc.).</li> <li>• <b>A financial institution that is guaranteed by the United Kingdom Government</b> (e.g. The Guaranteed Export Finance Company {GEFCO}) The security of interest and principal on maturity is on a par with the Government and so very secure, and these bonds usually provide returns above equivalent gilt edged securities. However the value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.</li> </ul>	AAA	Would not use in-house due to size of investment portfolio limiting benefit to authority.
2	<p><b>UK Gilt edged securities</b> with a maturity of greater than one year. These are Government bonds and so provide the highest security of interest and the repayment of principal on maturity. Similar to category (1) above, the value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.</p>	AAA Sovereign Rated	Not currently in use - requires approved Custodian to trade on our behalf
3	<p><b>Certificates of Deposit</b> with credit rated deposit takers (Banks and Building Societies)</p>	Sector Minimum Credit Worthiness rating	Not currently in use - requires approved Custodian to trade on our behalf
4	<p><b>Term deposit with a body which has been nationalised/part nationalised</b> by high credit rated (sovereign rating AAA) countries and provided with a <b>Government issued guarantee</b> for wholesale deposits within specific timeframes. Where these guarantees are in place and the government has an AAA sovereign long term rating these institutions will be included within the Council's criteria temporarily until such time as the ratings improve or the guarantees are withdrawn. Monies will only be deposited within the timeframe of the guarantee.</p>	AAA Sovereign Rated Sector Credit Worthiness rating 'Blue'	Under the current criteria this applies in the UK to Lloyds Banking Group plc and Royal Bank of Scotland Group institutions

	<b>Non Specified Investment Categories</b>	<b>Credit Rating</b>	<b>Comment</b>
5	A Term Deposit with a body which is an <b>Eligible Institution</b> for the HM Treasury Credit Guarantee Scheme initially announced on 13 <sup>th</sup> October 2008(1). The Credit Guarantee Scheme forms part of the Government's measures to ensure the stability of the financial system and protect ordinary savers, depositors, businesses and borrowers, by; a) providing sufficient liquidity in the short term, b) making available new capital to UK banks and Building Societies to strengthen their resources c) ensuring the banking system has the funds necessary to maintain lending in the medium term.	In accordance with Sector Credit Worthiness rating	Use restricted by Sector Credit Worthiness rating
6	Government guarantee on ALL deposits by high credit rated (AAA sovereign rating non UK) countries.	AAA Sovereign Rated	Not in Use, currently restricting investments to UK only
7	The <b>Council's Own Banker</b> if it fails to meet the basic credit criteria. In this instance balances will be minimised as far as possible.	Out of range	Currently fails to meet criteria, balances reviewed and minimised on daily basis
8	Any <b>Bank or Building society</b> that has at minimum a long term credit rating of A-, an Individual Rating of B/C and a Support rating of 3 or above, or equivalent, for deposits with a maturity of greater than one year (including forward deals in excess of one year from inception to repayment).	In accordance with Sector Credit Worthiness rating	Use restricted by Sector Credit Worthiness rating
9	<b>Callable Deposits</b> with a <b>Bank or Building society</b> that has at minimum a long term credit rating of A-, an Individual Rating of B/C and a Support rating of 3 or above, or equivalent.	In accordance with Sector Credit Worthiness rating	Use restricted by Sector Credit Worthiness rating
10	<b>Share capital or loan capital</b> in a body corporate – The use of these instruments will be deemed to be capital expenditure, and as such will be an application (spending) of capital resources. Revenue resources will not be invested in corporate bodies.	N/A	Unlikely to use due to size of portfolio and high risk associated. Also requires additional approval as deemed as capital expenditure.

Within categories 3, 4, 5 and 6, and in accordance with the Code, the Council has developed additional criteria to set the overall amount of monies which will be invested in these bodies. All investments will be made in sterling to eliminate exchange rate risk.

The criteria are detailed in the table below and will be used in conjunction with Sector's Creditworthiness service.

Counterparty Type (TBC's minimum credit ratings for approved lending list)	Minimum Credit Criteria	Limits*	
Bank or Building Society (a minimum Long Term Credit Rating of AAA, an Individual Rating of B/C and a Support rating of 3 (or equivalent))	Sector 'Yellow'	5 yrs	£4m
Bank or Building Society (a minimum Long Term Credit Rating of AA-, an Individual Rating of B/C and a Support rating of 3 (or equivalent))	Sector 'Yellow'	4 yrs	£4m
Bank (a minimum Long Term Credit Rating of A-, an Individual Rating of B/C and a Support rating of 3 (or equivalent))	Sector 'Yellow'	3 yrs	£4m
Banks Nationalised/Part nationalised by high credit rated (sovereign rating AAA) countries (a)	Sector 'Blue' (UK)	Specified in Guarantee	£4m
An Eligible Institution eligible under the HM Treasury Credit Guarantee Scheme (C)	Sector 'Blue'	Specified in Guarantee	£4m
Government guarantee on ALL deposits by high credit rated (AAA sovereign rating) countries (b).	Sector 'Blue'	Specified in Guarantee	£4m
The Council's own Banker - if it fails to meet basic criteria	n/a	Overnight	£2m
Building Society (a minimum Long Term Credit Rating of A- an Individual Rating of B/C and a Support rating of 3 (or equivalent /if applicable) AND assets > £4bn)	Sector 'Yellow'	3 yrs	£4m
Building Society (a Long Term Credit Rating of A- an Individual Rating of B/C and a Support rating of 3 (or equivalent/if applicable) AND assets < £4bn but > £1bn)	Sector 'Purple'	2 yrs	£4m
Group Limits - Maximum investments in Institutions within the same financial group	As above for individual investment	As above for individual investment	£6m
Territory Limits - Maximum investments in Institutions within the same Country (Approx 15% of investment programme) Non- UK	As above for individual investment	As above for individual investment	£2m
Territory Limits - Maximum investments in Institutions within the same Continent (Approx 30% of investment programme) Non UK	As above for individual investment	As above for individual investment	£4m

\* Under current Sector credit worthiness criteria, only institutions with a rating of 'Purple' or 'Yellow' are suggested as appropriate counterparties for investments over 1 year, with limit ranges of 2 years and 5 years respectively.

(a) **Nationalised/Part Nationalised Banks** in the UK have credit ratings which do not conform to the credit criteria usually used by local authorities to identify banks which are of high creditworthiness. In particular, as they no longer are separate institutions in their own right, it is impossible for Fitch to assign them an individual rating for their stand alone financial strength. Accordingly, Fitch has assigned an F rating which means that at a historical point of time, this bank failed and is now owned by the Government.

However, these institutions are now recipients of an F1+ short term rating as they effectively take on the creditworthiness of the Government itself i.e. deposits made with them are effectively being made to the Government. They also have a support rating of 1; in other words, on both counts, they have the highest ratings possible.

**(b) Blanket (explicit) guarantees on all deposits.** Some countries have supported their banking system by giving a blanket guarantee on ALL deposits e.g. Ireland and Singapore. Authorities may view that the sovereign rating of that country then takes precedence over the individual credit ratings for the banks covered by that guarantee.

**(c) UK banking system support package (implicit guarantee).** It should be noted that the UK Government did NOT give a blanket guarantee on all deposits but underlined its determination to ensure the security of the UK banking system by supporting eight named banks with a £500bn support package. The Council will need to decide if we wish to authorise lending to those named banks on the basis of that implicit guarantee on local authority deposits placed with these eight banks or to rely on the credit ratings of the individual banks.

The original list of banks covered when the support package was initially announced was: -

- . Abbey (now part of Santander)
- . Barclays
- . HBOS (now part of the Lloyds Group)
- . Lloyds TSB
- . HSBC
- . Nationwide Building Society
- . RBS
- . Standard Chartered

Banks eligible for support under the UK bail-out package and which have issued debt guaranteed by the Government are eligible for a continuing Government guarantee when debt issues originally issued and guaranteed by the Government mature and are refinanced. However, no other institutions can make use of this support as it closed to new issues and entrants on 28.2.10. The banks which have used this explicit guarantee are as follows: -

- . Bank of Scotland
- . Barclays
- . Clydesdale
- . Coventry Building Society
- . Investec bank
- . Nationwide Building Society
- . Rothschild Continuation Finance plc
- . Standard Life Bank
- . Tesco Personal Finance plc
- . Royal Bank of Scotland
- . West Bromwich Building Society
- . Yorkshire Building Society

**(d) Other countries.** The US, countries within the EU and Switzerland (and other countries) are currently providing major support packages to their banking systems.

## Approved Countries for Investments

### AAA

- Australia
- Canada
- Denmark
- Finland
- Germany
- Luxembourg
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland
- U.K.\*

\* At its meeting of the 15<sup>th</sup> September 2009, full Council approved a recommendation that;

***‘authorises the use of institutions currently supported by the UK Government should its Sovereign rating be downgraded below the current requirement for a ‘AAA’ rating by all three rating agencies’***

this approval continues to form part of the strategy in 2012/13.

## **Treasury Management Scheme of Delegation**

### **(i) Full Council**

- receiving and reviewing reports on Treasury Management policies, practices and activities,
- approval of annual strategy.
- approval of/amendments to the organisation's adopted clauses, Treasury Management Policy statement and Treasury Management practices.
- budget consideration and approval.
- approval of the division of responsibilities.
- receiving and reviewing regular monitoring reports and acting on recommendations.

### **(ii) Cabinet**

- receiving and reviewing Treasury Management policy statement and Treasury Management practices and making recommendations to the full Council.
- receiving and reviewing regular monitoring reports and making recommendations to the full Council.
- approving the selection of external service providers and agreeing terms of appointment.

### **(iii) Audit and Governance Committee**

- reviewing the Treasury Management policy and procedures and making recommendations to the Cabinet.
- receiving and reviewing regular monitoring (quarterly/half yearly) and making recommendations to the Cabinet.

## **The Treasury Management Role of the Section 151 Officer**

### **The S151 (responsible) Officer is responsible for:**

- recommending clauses, Treasury Management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- submitting regular Treasury Management policy reports;
- submitting budgets and budget variations;
- receiving and reviewing management information reports;
- reviewing the performance of the Treasury Management function;
- ensuring the adequacy of Treasury Management resources and skills, and the effective division of responsibilities within the Treasury Management function;
- ensuring the adequacy of internal audit, and liaising with external audit;
- recommending the appointment of external service providers.

## **TREASURY MANAGEMENT PRACTICES**

The Treasury Management Practices document (TMP's) forms detailed operational procedures and processes for the Treasury Management function. This document can be found on the Council's Internet by following the following link;

[http://www.tamworth.gov.uk/council\\_and\\_democracy/council\\_budgets\\_and\\_spending/treasury\\_management.aspx](http://www.tamworth.gov.uk/council_and_democracy/council_budgets_and_spending/treasury_management.aspx)

and clicking on the TMP's folder

The items below are summaries of the individual TMP's which the Council has to produce and adopt under the Treasury Code of Practice.

### **TMP1 : RISK MANAGEMENT**

#### **General Statement**

The Section 151 Officer will design, implement and monitor all arrangements for the identification, management and control of Treasury Management risk; will report at least annually on the adequacy / suitability of the arrangements and will report, as a matter of urgency, the circumstances of any actual or likely difficulty in achieving the Council's objectives. The reports will be in accordance with the procedures contained in TMP6.

#### **1.1 Credit and Counterparty Risk Management**

*Credit and counter-party risk is the risk of failure by a counterparty to meet its contractual obligations to the organisation under an investment, borrowing, capital project or partnership financing, particularly as a result of the counterparty's diminished creditworthiness, and the resulting detrimental effect on the organisation's capital or current (revenue) resources.*

This organisation regards a key objective of its Treasury Management activities to be the security of the principal sums it invests. Accordingly, it will ensure that its counterparty lists and limits reflect a prudent attitude towards organisations with which funds may be deposited, and will limit its investment activities to the instruments, methods and techniques referred to in TMP4 Approved Instruments Methods and Techniques and are detailed in the TMP Operational document.

It also recognises the need to have, and will therefore maintain, a formal counterparty policy in respect of those organisations from which it may borrow, or with whom it may enter into other financing arrangements.

#### **1.2 Liquidity Risk Management**

*This is the risk that cash will not be available when it is needed, that ineffective management of liquidity creates additional unbudgeted costs, and that the organisation's business/service objectives will be thereby compromised.*

This organisation will ensure it has adequate though not excessive cash resources, borrowing arrangements, overdraft or standby facilities to enable it at all times to have the level of funds available to it which are necessary for the achievement of its business/service objectives. This organisation will only borrow in advance of need where there is a clear business case for doing so and will only do so for the current capital programme or to finance future debt maturities.



### **1.3 Interest Rate Risk Management**

*The risk that fluctuations in the levels of interest rates create an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately.*

This organisation will manage its exposure to fluctuations in interest rates with a view to containing its interest costs, or securing its interest revenues, in accordance with the amounts provided in its budgetary arrangements as amended in accordance with TMP6 Reporting requirements and management information arrangements.

It will achieve this by the prudent use of its approved financing and investment instruments, methods and techniques, primarily to create stability and certainty of costs and revenues, but at the same time retaining a sufficient degree of flexibility to take advantage of unexpected, potentially advantageous changes in the level or structure of interest rates. This should be the subject to the consideration and, if required, approval of any policy or budgetary implications.

### **1.4 Exchange Rate Risk Management**

*The risk that fluctuations in foreign exchange rates create an unexpected or unbudgeted burden on the organisation's finances, against which the organisation has failed to protect itself adequately.*

It will manage its exposure to fluctuations in exchange rates so as to minimise any detrimental impact on its budgeted income/expenditure levels.

### **1.5 Refinancing Risk Management**

*The risk that maturing borrowings, capital, project or partnership financings cannot be refinanced on terms that reflect the provisions made by the organisation for those refinancing, both capital and current (revenue), and/or that the terms are inconsistent with prevailing market conditions at the time.*

This organisation will ensure that its borrowing, private financing and partnership arrangements are negotiated, structured and documented, and the maturity profile of the monies so raised are managed, with a view to obtaining offer terms for renewal or refinancing, if required, which are competitive and as favourable to the organisation as can reasonably be achieved in the light of market conditions prevailing at the time.

It will actively manage its relationships with its counterparties in these transactions in such a manner as to secure this objective, and will avoid over reliance on any one source of funding if this might jeopardise achievement of the above.

### **1.6 Legal and Regulatory Risk Management**

*The risk that the organisation itself, or an organisation with which it is dealing in its Treasury Management activities, fails to act in accordance with its legal powers or regulatory requirements, and that the organisation suffers losses accordingly.*

This organisation will ensure that all of its Treasury Management activities comply with its statutory powers and regulatory requirements. It will demonstrate such compliance, if required to do so, to all parties with whom it deals in such activities. In framing its credit and counterparty policy under TMP1[1] credit and counterparty risk management, it will ensure that there is evidence of counterparties' powers, authority and compliance in respect of the transactions they may effect with the organisation, particularly with regard to duty of care and fees charged.

This organisation recognises that future legislative or regulatory changes may impact on its Treasury Management activities and, so far as it is reasonably able to do so, will seek to minimise the risk of these impacting adversely on the organisation.

## **1.7 Fraud, Error and Corruption, and Contingency Management**

*The risk that an organisation fails to identify the circumstances in which it may be exposed to the risk of loss through fraud, error, corruption or other eventualities in its Treasury Management dealings, and fails to employ suitable systems and procedures and maintain effective contingency management arrangements to these ends. It includes the area of risk commonly referred to as operational risk.*

This organisation will ensure that it has identified the circumstances which may expose it to the risk of loss through fraud, error, corruption or other eventualities in its Treasury Management dealings. Accordingly, it will employ suitable systems and procedures, and will maintain effective contingency management arrangements, to these ends.

The Council will therefore:-

- a) Seek to ensure an adequate division of responsibilities and maintenance at all times of an adequate level of internal check which minimises such risks.
- b) Fully document all its Treasury Management activities so that there can be no possible confusion as to what proper procedures are.
- c) Staff will not be allowed to take up Treasury Management activities until they have had proper training in procedures and are then subject to an adequate and appropriate level of supervision.

Records will be maintained of all Treasury Management transactions so that there is a full audit trail and evidence of the appropriate checks being carried out.

## **1.8 Market Risk Management**

*The risk that, through adverse market fluctuations in the value of the principal sums an organisation borrows and invests, its stated Treasury Management policies and objectives are compromised, against which effects it has failed to protect itself adequately.*

This organisation will seek to ensure that its stated Treasury Management policies and objectives will not be compromised by adverse market fluctuations in the value of the principal sums it invests, and will accordingly seek to protect itself from the effects of such fluctuations.

## **TMP2 : BEST VALUE AND PERFORMANCE MEASUREMENT**

The Borough Council is committed to the pursuit of best value in its Treasury Management activities, and to the use of performance methodology in support of that aim, within the framework set out in the Treasury Management Policy Statement.

The Treasury Management function will be the subject of ongoing analysis of the value it adds in support of the Council's stated service objectives. It will be the subject of regular examination of alternative methods of service delivery, of the availability of fiscal, grant or subsidy incentives, and the scope for other potential improvements. The performance of the Treasury Management function will be measured using the criteria set out in the detailed TMP Operational document.

### **TMP3 : DECISION-MAKING AND ANALYSIS**

The Council will maintain full records of its Treasury Management decisions, and of the processes and practices applied in reaching those decisions, both for the purposes of learning from the past, and for demonstrating that reasonable steps were taken to ensure that all issues relevant to those decisions were taken into account at the time. The issues to be addressed and processes and practices to be pursued in reaching decisions are set out in the detailed TMP Operational document.

### **TMP4 : APPROVED INSTRUMENTS, METHODS AND TECHNIQUES**

The Council will undertake its Treasury Management activities by employing only those instruments, methods and techniques which are set out in the detailed TMP Operational document and within the limits and parameters defined in TMP1.

### **TMP5 : ORGANISATION, CLARITY AND SEGREGATION OF RESPONSIBILITIES, AND DEALING ARRANGEMENTS**

The Council considers it essential, for the purposes of the effective control and monitoring of its Treasury Management activities, for the reduction of risk of fraud or error, and for the pursuit of optimum performance, that these activities are structured and managed in a fully integrated manner, and that there is at all times clarity of Treasury Management responsibilities.

The principle, on which this will be based is the clear distinction between those charged with setting Treasury Management policies and those charged with implementing and controlling these policies, particularly with regard to the execution and transmission of funds, the recording and administering of Treasury Management decisions and the audit and review of the Treasury Management function.

If and when this organisation intends, as a result of lack of resources or other circumstances, to depart from these principals, the Section 151 Officer will ensure that the reasons are properly reported in accordance with TPM6 and the implications properly considered and evaluated.

The Section 151 Officer will ensure that there are clear written statements of the responsibilities for each post engaged in Treasury Management, and the arrangements for absence cover. He will also ensure that at all times those engaged in Treasury Management will follow the policies and procedures set out. The present arrangements are set out in the detailed TMP Operational document.

The Section 151 Officer will ensure that there is proper documentation for all deals and transactions, and that procedures exist for the effective transmission of funds. The present arrangements are set out in the detailed TMP Operational document.

The delegations to the Section 151 Officer in respect of Treasury Management are set out in the detailed TMP Operational document.

He will fulfil all such responsibilities in accordance with the Council's policy statement and TMP's and, if a CIPFA member, the Standard of Professional Practice on Treasury Management.

## **TMP6 : REPORTING REQUIREMENTS AND MANAGEMENT INFORMATION ARRANGEMENTS**

The Council will ensure that regular reports are prepared and considered on the implementation of its Treasury Management policies; on the effects of decisions taken and transactions executed in pursuit of those policies; implications of changes, particularly budgetary, resulting from regulatory, economic, market or other factors affecting its Treasury Management activities; and on the performance of the Treasury Management function.

As a minimum Cabinet and Council will receive:

- An annual report on the planned strategy to be pursued in the coming year and the reporting of Prudential Indicators.
- A mid-year review
- An annual report on the performance of the Treasury Management function including the performance against the Prudential Indicators, the effects of the decisions taken and the transactions executed in the past year and on any circumstances of non-compliance with the Council's Treasury Management policy statement and TMP's.

Cabinet will receive regular monitoring reports on Treasury Management activities and risks.

The Audit and Governance Committee will have responsibility for the scrutiny of Treasury Management policies and practices.

The Treasury Management indicators will be considered together with the Treasury Management indicators in the Prudential Code as part of the budget approval process. The present arrangements and the form of these reports are set out in the detailed TMP Operational document.

## **TMP7 : BUDGETING, ACCOUNTING AND AUDIT ARRANGEMENTS**

The Section 151 Officer will prepare and Council will approve and, if necessary, from time to time will amend, an annual budget for Treasury Management, which will bring together all of the costs involved in running the Treasury Management function together with associated income. The matters to be included will at minimum be those required by statute or regulation, together with such information as will demonstrate compliance with TMP1, TMP2 and TMP4.

The Section 151 Officer will exercise effective controls over this budget and report upon and recommend any changes required in accordance with TMP6.

The Council will account for its Treasury Management activities, for decisions made and transactions executed in accordance with appropriate accounting practices and standards, and with statutory and regulatory requirements in force for the time being.

## **TMP8 : CASH AND CASH FLOW MANAGEMENT**

Unless statutory or regulatory requirements demand otherwise, all monies in the hands of the Council will be under the control of the Section 151 Officer and will be aggregated for cash flow and investment management purposes. Cash flow projections will be prepared on a regular and timely basis and the Section 151 Officer will ensure that these are adequate for the purpose of monitoring compliance with TMP1. The present arrangements for preparing cash flow projections, and their form, are set out in the detailed TMP Operational document.

## **TMP9 : MONEY LAUNDERING**

The Council is alert to the possibility that it may become the subject of an attempt to involve it in a transaction involving the laundering of money. The Council will, therefore, maintain procedures for verifying and recording the identity of counterparties and reporting suspicions, and will ensure that all staff involved are properly trained. The present arrangements, including the name of the officer to whom reports should be made, are set out in the detailed TMP Operational document.

## **TMP10 : TRAINING AND QUALIFICATIONS**

The Council recognises the importance of ensuring that all staff involved in the Treasury Management function are fully equipped to undertake the duties and responsibilities allocated to them. It will seek to appoint individuals, who are both capable and experienced and will provide training for staff to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills. The Section 151 Officer will recommend and implement the necessary arrangements.

The Section 151 Officer will ensure that Council members tasked with Treasury Management responsibilities, including those responsible for scrutiny, have access to training relevant to their needs and those responsibilities.

Those charged with governance recognise their individual responsibility to ensure that they have the necessary skills to complete their role effectively.

## **TMP11 : USE OF EXTERNAL SERVICE PROVIDERS**

The Council recognises that responsibility for the Treasury Management decisions remains with the Council at all times. It recognises that there may be potential value in employing external providers of Treasury Management services, in order to acquire access to specialist skills and resources. When it employs such service providers, it will ensure it does so for reasons, which will have been submitted to a full evaluation of the costs and benefits. Terms of appointment will be properly agreed, documented and subject to regular review. It will ensure, where feasible and necessary, that a spread of service providers is used, to avoid over reliance on one or a small number of companies. Where services are subject to formal tender or re-tender arrangements, legislative requirements will always be observed. The monitoring of such arrangements rests with the Section 151 Officer, and details of the current arrangements are set out in the detailed TMP Operational document.

## **TMP12 : CORPORATE GOVERNANCE**

The Council is committed to the pursuit of proper corporate governance throughout its services, and to establishing the principles and practices by which this can be achieved. Accordingly the Treasury Management function and its activities will be undertaken with openness, transparency, honesty, integrity and accountability.

The Council has adopted and implemented the key recommendations of the Code. This, together with the other arrangements are set out in the detailed TMP Operational document and are considered vital to the achievement of proper governance in Treasury Management, and the Section 151 Officer will monitor and, if and when necessary, report upon the effectiveness of these arrangements.

## Treasury Management Glossary of Terms

Bank Rate	The Official Bank rate paid on commercial bank reserves i.e. reserves placed by commercial banks with the Bank of England as part of the Bank's operations to reduce volatility in short term interest rates in the money markets.
Base Rate	Minimum lending rate of a bank or financial institution in the UK.
Capital Financing Requirement	The Council's underlying need for borrowing for a capital purpose.
Counterparty	The organisations responsible for repaying the Council's investment upon maturity and for making interest payments.
Credit Default Swap (CDS)	A specific kind of counterparty agreement which allows the transfer of third party credit risk from one party to the other. One party in the swap is a lender and faces credit risk from a third party, and the counterparty in the credit default swap agrees to insure this risk in exchange of regular periodic payments (essentially an insurance premium). If the third party defaults, the party providing insurance will have to purchase from the insured party the defaulted asset. In turn, the insurer pays the insured the remaining interest on the debt, as well as the principal.
Credit Rating	This is a scoring system that lenders issue organisations with, to determine how credit worthy they are.
Gilts	These are issued by the UK Government in order to finance public expenditure. Gilts are generally issued for a set period and pay a fixed rate of interest for the period.
iTraxx	This is an index published by Markit who are a leading company in CDS pricing and valuation. The index is based on an equal weighting of the CDS spread of 25 European financial companies. Clients can use the iTraxx to see where an institutions CDS spread is relative to that of the market and judge its creditworthiness in that manner, as well as looking at the credit ratings.
Liquidity	An asset is perfectly liquid if one can trade immediately, at a price not worse than the uninformed expected value, the quantity one desires.
Long term	A period of one year or more.
Maturity	The date when an investment is repaid or the period covered by a fixed term investment.

Minimum Revenue Provision	Capital expenditure is generally expenditure on assets which have a life expectancy of more than one year e.g. buildings, vehicles, machinery etc. It would be impractical to charge the entirety of such expenditure to revenue in the year in which it was incurred therefore such expenditure is spread over several years in order to try to match the years over which such assets benefit the local community through their useful life. The manner of spreading these costs is through an annual Minimum Revenue Provision
Monetary Policy Committee (MPC)	This is a body set up by the Government in 1997 to set the 'Repo' rate (commonly referred to as being base rate). Their primary target (as set by the Government) is to keep inflation at or around a 2%.
Security	An investment instrument, issued by a corporation, government, or other organization which offers evidence of debt or equity.
Short Term	A period of 364 days or less
S.L.Y	The Authority's risk appetite is low in order to give priority to <b>S</b> ecurity, <b>L</b> iquidity then <b>Y</b> ield (or return on investments)
Treasury Management	The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.
Working Capital	Cash and other liquid assets needed to finance the everyday running of a business such as the payment of salaries and purchases.
Yield	The annual rate of return on an investment, expressed as a percentage.